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STATE FOR WHA, WHA/CEN, WHA/EPSC, EEB/CBA, EEB/IEC  
STATE PASS TO OPIC  
USDOC FOR 4332/ITA/MAC/WH/MSIEGELMAN  
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E.O. 12958: DECL: 05/11/2017  
TAGS: [EPET](#) [EINV](#) [ECON](#) [PREL](#) [NU](#)  
SUBJECT: NICARAGUA: OIL CONCESSIONS TO U.S. COMPANIES  
CAUGHT IN JUDICIAL LIMBO

REF: MANAGUA 285

Classified By: Ambassador P. Trivelli for reasons 1.4 b&d.

¶1. (C) Summary: On 10 August, 2006, a court in the Southern Autonomous Atlantic Region (RAAS) accepted a writ of injunction/relief against the Attorney General for signing oil exploration concessions with two U.S. companies without having properly consulted with the governments of the Autonomous Atlantic Regions (RAAN and RAAS). The Supreme Court must now decide whether the Attorney General acted improperly. The Attorney General, the companies, and the energy regulator all filed responses to the case stating that the concessions were issued within the framework of Law 445 limiting RAAN and RAAS authority over Caribbean waters.

¶2. (C) The Ambassador has discussed the situation with the Vice-President, the Foreign Minister, and the Minister of Energy, without resolution. While the new Minister of Energy, who now has authority over concessions, says the contracts are proper, the Attorney General and FM assert that the oil companies must still win approval from the RAAN and RAAS governments. MKJ's lawyers believe there may be some Sandinistas using the case to cancel the concessions and hand them over to Venezuela. While recent visits by MKJ and Infinity have elicited positive responses from GON, RAAN, and RAAS leaders, it is clear the companies are caught in Sandinista efforts to curry favor with the Atlantic coast. End Summary.

#### Background on Concessions

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¶2. (U) In April 2006, two U.S. companies, MKJ International and Infinity Energy each signed oil exploration concession agreements with the GON after completing six years of negotiations. This process included extended negotiations with the RAAN and RAAS Directive Councils (governments), as the concessions were off Nicaragua's Caribbean coast. Law 445, passed during negotiations in 2003, limited RAAN/RAAS authority over Nicaragua's Caribbean waters to three miles from the coast and 25 miles around any islands. This legislation essentially shifted the MKJ and Infinity concessions to national waters and freed the companies to negotiate only with the central government. Changes in the energy regulator in 2005 further delayed the negotiations and approval process. In April 2006, the Attorney General finally signed the concession agreements in the name of the

President, granting the companies six years to complete environmental impact statements, geological soundings, and commence exploration. The contracts also incorporate a 30-year production sharing agreement should exploration prove successful. U.S. publicly traded Nobel Energy will participate in the MKJ project.

#### The Case

13. (C) On 10 August, 2006 a court in Bluefields (RAAS) accepted a writ of injunction/relief against the Attorney General for signing the concessions without having properly consulted with the RAAS and RAAN Directive Councils. The petitioners are Sandinistas, as is their attorney. Once the writ was accepted, it moved to the Supreme Court (CSJ) which must determine if the Attorney General acted improperly and the injunction is therefore valid. The CSJ accepted the case within the 60-day limit, but has not issued a final decision on the injunction. There is no time limit for the CSJ to issue such a decision (reftel).

14. (SBU) At the end of August, the Attorney General filed a response to the writ and MKJ and Infinity presented papers as "parties affected." The National Institute of Energy (INE), the energy regulator and chief GON negotiator of the concessions, sent the Attorney General additional evidence to support the GON's position that the concessions were properly completed with the required consultations. The Attorney General never presented the additional evidence to the CSJ.

15. (SBU) All the documents state that the concessions were issued within the framework of law 445; meaning that the writ of injunction has no legal basis. Maps included in the papers demonstrate that the concessions were drawn to ensure that they were in national waters, outside of the RAAN/RAAS 25 mile administrative zone. Thus, consultations with, and approval from, the Directive Councils were not required.

#### Actions since August

16. (SBU) While the injunction stopped MKJ and Infinity's ability to complete the environmental impact statements and begin seismic testing, it did not automatically stop the six year concession clock. In November, when it became clear that the CSJ was not going to move quickly, INE halted the clock by suspending the concessions, pending resolution of the case.

17. (SBU) The Ambassador discussed this case with the outgoing Bolanos administration and with the current Vice-President, Foreign Minister, and Minister, Vice-Minister and Secretary General of Energy (newly created ministry assuming concession responsibilities from INE). According to Vice Minister of Energy Lorena Lanza Espinosa, Minister of Energy Emilio Rapaccoli personally reviewed MKJ and Infinity's contracts and declared them to be proper. The Ministry, therefore, stands by the concessions but claims it cannot take any action while the case is in the CSJ. It is up to the Attorney General's office to defend the GON's position. (Note: During a meeting with Infinity, the Attorney General stated that while he cannot tell the CSJ what to do, he has also not told them so far what decision to make. End note.)

#### A Possible Wrinkle

18. (C) VM Lanza did raise a possible loophole the CSJ could use to declare the writ of injunction valid and allow for a possible cancellation of the concessions. While the negotiations concluded under the terms of Law 445, they began while the RAAN/RAAS still exercised authority over Caribbean waters. Under previous laws, INE was required to announce the conclusion of the negotiations and begin a 60-day public comment period. During such a period the RAAN and RAAS Directive Councils could have raised concerns that would have been addressed before the concessions were signed. As such

consultations do not apply under Law 445 because the concessions are outside RAAN/RAAS waters the 60-day notice period did not place. The CSJ may say it should have because the negotiations began under the old laws.

#### The Sandinista Angle

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¶9. (C) Attorney General Hernan Estrada and Foreign Minister Samuel Santos suggested to MKJ and Infinity that it would be helpful if they gain formal approval on the concessions from the RAAN/RAAS Directive Councils. The FM told Infinity that the GON is "focused on giving the communities a little more."

He stated that the concession contracts may need to be "fixed around the edges" to increase assistance to RAAN/RAAS.

The Chief Justice of the CSJ told MKJ's lawyers that he has been directed to hold off on any action on the writ until RAAN and RAAS issue approvals. MKJ's lawyers believe that the Ortega Administration is trying to re-extend RAAN/RAAS authority over all the Nicaraguan Caribbean waters as a way to curry favor with the strongly anti-Sandinista regions. By making MKJ and Infinity obtain official RAAN/RAAS approval, the Sandinistas could create a defacto granting of such authority, even though it contradicts existing law. Secretary General of Energy Donald Espinosa, one of the lead negotiators of the concessions for INE, told econoff that such a position could jeopardize "serious" interest in future bid solicitations for the remaining concessions in Nicaragua's Caribbean waters.

¶10. (SBU) The RAAN and RAAS Directive Councils have made no public pronouncements on the case. Both MKJ and Infinity have visited the regions to assess the situation. They found Directive Councils upset with the GON at being excluded from the concession process, but very supportive of the projects and the companies. Informal conversations have circled around the RAAN and RAAS getting higher royalties at the back end of the deals, but nothing is on paper. The law is not clear on whether such agreements can be done directly with the councils or must go through the Ministry of Energy. Both Directive Councils have promised to have the full RAAN and RAAS Councils vote on the concessions in the near future.

#### OPIC's Role

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¶11. (C) MKJ and Infinity both have OPIC political risk insurance for their concessions, which the companies could invoke as early as September 2007. According to OPIC, the current writ of injunction can be interpreted as a de-facto expropriation and the companies could receive payment. In such a situation, OPIC would re-evaluate its position in Nicaragua. OPIC changing its risk assessment on Nicaragua could lead to Ex-Im and private banks increasing their risk evaluations, making money for investment in Nicaragua more expensive and limiting new projects.

#### A possible Venezuela Angle

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¶12. (C) MKJ's lawyers have suggested that the writ may actually be a legal ploy by some Sandinistas to cancel the concessions so they can be handed over to Venezuela's PDVSA. They claim to have been asked if MKJ would consider jointly exploiting the concession with PDVSA. During post and Infinity's separate meetings with the GON, such a suggestion has never been raised.

#### Comment

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¶13. (C) It is becoming increasingly clear that MKJ and Infinity are caught in Sandinista efforts to curry favor with the Atlantic coast. While the GON members willing to discuss the case have all been supportive of the companies, it is clear they are unwilling to move until the RAAN and RAAS approve the concessions. However, the GON's short-term focus on winning over the Atlantic coast is blinding it to the

long-term costs of these actions. Giving the RAAN and RAAS Directive Councils a voice in the negotiation of concession contracts increases the work and time these will take, likely dissuading potential bidders on any future bid solicitations for the 100-plus remaining Caribbean blocks. Additionally, should Nicaragua be seriously considering giving PDVSA a central role in the concessions, the GON might be surprised at PDVSA's limited exploration capability. The GON would do better to take swift action to advance the U.S. companies' concessions so that if oil is discovered, other foreign companies would want to come to Nicaragua to explore. End comment.

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